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Dollar onus falls on Japan

The Bank of Japan can be expected to stage a strong defense of the dollar in the months ahead.

The meeting of the Group of Seven (G-7) finance ministers and central bankers in Washington on April 13 was meant to be a holding operation. In the event the statement issued at the end of the meeting succeeded in holding the U.S. dollar for less than 24 hours.

The U.S. trade figures for February, showing a deficit of $13.8 billion, sent the dollar sharply lower. Currency market reaction would have been even more extreme had not the G-7 central banks intervened in force to stem the dollar's decline.

What was remarkable about the action on the foreign exchanges was not so much that the dollar fell—the U.S. dollar is likely to remain under downward pressure for as long as the U.S. productive sector continues to shrink relative to the productive sectors of other countries—but that this particular decline should be triggered by an event of relatively minor significance in itself.

The merchandise trade figures are an erratic statistical series. In several previous months, they have turned out better than the market generally had expected. The figures released on April 14, however, happened to be $2 billion worse than market expectations. This fluctuation was enough to put the skids under the dollar.

Clearly, market confidence in continuing currency stability is much more fragile than it seemed to be earlier this year. The G-7 central banks will be in for a torrid time supporting the U.S. currency ahead of the presidential election. And yet, they cannot allow the dollar to slip, for this could, this year, develop into a particularly dangerous "free fall."

This is because the foreign exchanges perceive that the U.S. administration is winding down and would be powerless to step in with measures and promises to support the U.S. dollar, as it did last summer.

The key flow supporting the U.S. currency is the inflow into U.S. assets from Japan. The evidence is that, despite some pick-up in Japanese private sector investment in U.S. stocks and bonds since the fourth quarter of 1987, Japanese public sector flows into the U.S.A., in the shape of Bank of Japan intervention to support the dollar, will have to be substantial in the months ahead if the dollar is to remain steady.

While other G-7 central banks are also likely to be willing to support the dollar, there are limits to how far the West German Bundesbank and the Bank of England are prepared to go. This leaves the onus of dollar support on the Bank of Japan.

There is a constraint on the Bank of Japan's intervention. This is the potential inflationary impact of dollar-support buying which comes about through the upward pressure which the support exerts on the liquidity in Japanese domestic credit markets.

On the other hand, the Bank of Japan will calculate that, if the U.S. dollar is allowed to collapse during a U.S. presidential election year, the new U.S. administration would almost certainly be impelled to adopt protectionist trade measures which would damage Japan's interests.

On balance, it seems likely that the Bank of Japan will take risks with excess domestic liquidity if this means avoiding adverse political developments in the U.S.A. Consequently, the Bank of Japan can be expected to stage a strong defense of the dollar in the months ahead.

The result of this will be a further build-up of dollar assets in Japanese official hands. This fits in with Japan's longer-term aim of strengthening its control over U.S. economic activity.

Czechoslovakia, by East bloc standards, is considered "fortunate" in terms of housing and living standards. As will be clear from the picture we present, only from a Romanian or Polish yardstick can this adjective be used.

1) By the end of 1984, 580,000 Czechoslovakian families had *no* apartment of their own.

2) Forty percent of families have apartments with less than 8 square meters (8½ square yards) per person. The average space of an apartment built in 1984 was 46.3 square meters (50 square yards).

3) Of some 5 million apartments in Czechoslovakia, 1,172,000 of them, more than 20%, have no private toilet facilities.

In East Germany, the so-called apartment paradise of the East bloc, in 1984, 28% of all apartments had neither bath nor shower facilities.

Nothing, of course, matches the dimensions of the housing crisis in Poland. The young generation of people in their twenties lives without the hope of having their own apartment until they are well into their forties. Add this to the daily shortages or lack of basic essentials, and ever-increasing prices for food and fuel, and it is only a matter of time before Moscow and Jaruzelski have another Polish crisis on their hands.